IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

UNITED STATES OF AMERICA,

v.

Case No. CR-03-BE-0530-S

RICHARD M. SCRUSHY,

Defendant.

DEFENDANT RICHARD M. SCRUSHY'S
CONSOLIDATED REPLY MEMORANDUM IN
FURTHER SUPPORT OF NON-DISPOSITIVE MOTIONS

Abbe David Lowell
Thomas V. Sjoblom
Scott S. Balber

CHADBOURNE & PARKE LLP
1200 New Hampshire Avenue, N.W.
Washington, D.C. 20036

and

Arthur W. Leach

c/o THOMAS, MEANS, GILLIS & SEAY, P.C.
505 20th Street North
Birmingham, Alabama 35237

Counsel for Defendant Richard M. Scrushy

TABLE OF CONTENTS

IN THE UNITED STATES DISTRICT COURT
FOR THE NORTHERN DISTRICT OF ALABAMA
SOUTHERN DIVISION

UNITED STATES OF AMERICA,

v.

Case No. CR-03-BE-0530-S

RICHARD M. SCRUSHY,

Defendant.

DEFENDANT RICHARD M. SCRUSHY'S
CONSOLIDATED REPLY MEMORANDUM IN
FURTHER SUPPORT OF NON-DISPOSITIVE MOTIONS

Defendant Richard M. Scrushy respectfully submits this Consolidated Reply Memorandum in Further Support of his Non-Dispositive Motions filed on January 26, 2004.

PRELIMINARY STATEMENT

While the relief sought by Mr. Scrushy in his seven non-dispositive motions relates to wide ranging subject matter, the Government's consolidated response (the "Opp. Br.") is remarkably uniform in its approach -- it seeks to reiterate repeatedly the broadbased, ambiguous and highly inflammatory allegations set forth in the Indictment (sometimes gratuitously arguing, for public consumption, how "guilty" Mr. Scrushy is)

while jealously guarding the alleged facts and evidence that purportedly support these charges. Rather than countenance this hide and seek tactic, this Court should begin the process of requiring the Government to abide by the obligations imposed on it by the Constitution and the Federal Rules of Criminal Procedure.

ARGUMENT

I. Mr. Scrushy Is Entitled To A Bill Of Particulars

In response to Mr. Scrushy's demand for a bill of particulars, the Government confuses a defendant's right to know the precise nature of the charges against him with a request for discovery of the particularized evidentiary details that the Government will attempt to use to prove those charges. Opp. Br. at 8. Mr. Scrushy seeks (and is entitled to) only the former. United States v. Warren, 772 F.2d 827, 837 (11th Cir. 1985).

The Government recognizes its obligation to inform Mr. Scrushy "of the charge against him with sufficient precision to allow him to prepare his defense, to minimize surprise at trial, and to enable him to plead double jeopardy in the event of a later prosecution of the same offense" (Opp. Br. at 5 (quoting Warren, 772 F.2d at 837)) and seeks to fulfill this obligation by "laboriously describ[ing] in sixteen paragraphs the manner and means of the conspiracy." Opp. Br. at 6. However, the Government's compliance with Warren can be achieved based on the quality, not the quantity of the disclosure. Six or sixty vague paragraphs make no difference. The Government claims that the Indictment sets forth some, but not all, of the alleged meetings with co-conspirators and false statements made to regulators and in furtherance of the conspiracy.

Opp. Br. at 7. But Mr. Scrushy is entitled to know the precise nature of all of the charges against him so that he can prepare a defense to each (not just some) of the alleged false statements and conspiratorial meetings that form the basis for the Indictment. Absent such specificity it would be impossible, for double jeopardy purposes, to determine which alleged criminal acts are encompassed in the Indictment and which are not. And the Government fails to note that even sufficiently explaining the "manner and means of the conspiracy" is not enough to meet its burden because "conspiracy" is only one of eighty five counts in the Indictment.[1]

The Government claims that "the voluminous discovery already provided gives Scrushy sufficient information from which to prepare his defense and to plead double jeopardy." Opp. Br. at 7. However, the necessity of a bill of particulars is only increased, not abated, by the voluminous documents produced by the Government in this case. The Government does not "fulfill its obligations merely by providing mountains of documents to defense counsel" where defense counsel are "left unguided as to which documents would be proven falsified. . . ." United States v. Bortnovsky, 820 F.2d 572, 575 (2nd Cir. 1987). In Bortnovsky, the Court of Appeals for the Second Circuit reversed the defendants' convictions because the lower court denied the defendants'

---

[1] In this regard, the Government's contention that "an indictment for conspiracy need not be as specific as an indictment for a substantive count," even if true, far from carries the day on the other eighty-four counts. Opp. Br. at 6.

motion for a bill of particulars seeking information regarding which documents were allegedly falsified. The Court rejected the Government's contention that it had met its obligations by producing over 4,000 documents, some of which were allegedly falsified. Id. at 574. The Court found the defendants were "hindered in preparing their defense" by the Government's failure to provide the requested information. Id. A defendant's right to know the specifics of his alleged offense is met by a bill of particulars, United States v. Panzavecchia, 421 F.2d 440, 442 (5th Cir. 1970), not by being forced to guess which of the millions of documents and other discovery materials the government believes add clarity to the vague allegations in the Indictment.

Finally, the Government concedes that is must provide Mr. Scrushy with a list of co-conspirators it may call at trial, but it resists identifying unnamed co-conspirators, unnamed aiders and abettors, officers, members of the corporate accounting staff and others who are referred to, but left unidentified, whether the Government intends to call these individuals as witnesses at trial or not. Opp. Br. at 8-9. There is no principled reason for the distinction the Government seeks to draw. Rather, the United States Supreme Court has found that it is appropriate for the Government to be compelled to produce names of individuals where the information will be useful in the defendant's trial preparation. Will v. United States, 389 U.S. 90, 99 (1967) ("[I]t is not uncommon for the Government to be required to disclose the names of some potential witnesses in a bill of particulars, where this information is necessary or useful in the defendant's preparation

for trial."). The Government chose to refer to these individuals in the Indictment and should not now be permitted to hide from those same allegations.

II. This Court Should Strike Surplusage From The Indictment

As the Government acknowledges, pursuant to Fed. R. Crim. P. 7(c)(1), an indictment must contain a "plain, concise and definite written statement of the essential facts constituting the offense charged." Opp. Br. at 9. But there is nothing plain, concise or definite about this Indictment. And it includes numerous allegations that are by no means essential to the offenses charged.

In its opposition to Mr. Scrushy's motion to strike surplusage, the Government has conflated several distinct issues -- what may be appropriately alleged in an indictment, what may be appropriately admitted into evidence and what may be appropriately charged to the jury. The Government suggests that surplusage should not be stricken from the Indictment because the Court may address improper allegations by preventing the Government from offering evidence in support of those allegations or through curative instructions to the jury. Opp. Br. at 13. By this logic, however, the Court should never strike surplusage from an Indictment because subsequent procedural mechanisms can cure all wrongs. Numerous courts in this Circuit and elsewhere, however, have recognized the importance of striking surplusage from an indictment without regard to what the Government may concede in trial proof or ultimate instructions. See, e.g., United States v. Bissell, 866 F.2d 1343, 1355-56 (11th Cir. 1989);

United States v. Hughes, 766 F.2d 875, 879 (5th Cir. 1985); United States v. Poore, 594 F.2d 39, 41-43 (4th Cir. 1979).

A. References to Mr. Scrushy's "Fiduciary Duties" Should Be Stricken From The Indictment

The Government asserts that "Scrushy moves to strike the following *bland* reference from paragraph 2 of the indictment: 'Richard M. Scrushy was the highest ranking corporate officer responsible for overall management of the company, and he owed a fiduciary duty to render honest services to HealthSouth, its shareholders, and its Board of Directors.'" Opposition Brief at 10-11 (emphasis added). However, blandness is in the eye of the beholder and the Government has proven, with its extrajudicial statements and gratuitous inclusion of inflammatory language in its filings, that it should not be the arbiter of what is proper.[2] There is no principled reason to include a reference to Mr. Scrushy's alleged fiduciary duties in the Indictment in order to meet the Government's burden of proving a violation of 18 U.S.C. § 1346. But reference to a duty giving rise to civil, rather than criminal, liability unnecessarily creates the potential of confusing the jury.

By the plain meaning of the statute, an individual need not breach a fiduciary duty -- and need not be "the highest ranking corporate officer responsible for overall

---

[2] Query why the Government spills more than two pages of ink defending such a purportedly "bland" allegation. Opp. Br. at 10-12.

management of the company" -- to be convicted of violating 18 U.S.C. § 1346. The statute states:

> For the purposes of this chapter, the term "scheme or artifice to defraud" includes a scheme or artifice to deprive another of the intangible right of honest services.

Nothing in the statute requires the Government to prove that Scrushy owed a fiduciary duty to HealthSouth. See, e.g., United States v. Sancho, 957 F. Supp. 39, 42 (S.D.N.Y. 1997) ("There is simply no indication from the text of §§ 1343 and 1346 that a necessary element of wire fraud is the existence of an actual fiduciary duty."), aff'd, 157 F.3d 918, 920 (2d Cir. 1998) ("Nothing in either § 1343 or § 1346 indicates that the existence of an actual fiduciary duty is a necessary element of the crime. These statutes make it a crime to devise a *scheme* to deprive another of the right of honest services."). Accordingly, by simply being an employee of HealthSouth, Scrushy owed HealthSouth "the intangible right of honest services." Thus, any references in the Indictment to Mr. Scrushy having some special or other fiduciary duty to HealthSouth are surplusage.

The Government's description of Mr. Scrushy's position in the company -- namely, that he was "the highest ranking corporate officer responsible for overall management of the company," and "owed fiduciary duties to" it -- is prejudicial because it suggests that, for purposes of the offense charged, he owed greater duties to HealthSouth than anyone else and thus his conduct need not be as severe as others to "deprive [HealthSouth] of the intangible right of honest services." This simply is not true, however. What is alleged to be criminal conduct by Scrushy vis-à-vis his activities

at HealthSouth would also be deemed criminal conduct if it was performed by any other employee at HealthSouth. All that is necessary is "a *scheme* to deprive another of the right of honest services." Sancho, 157 F.3d at 920. The presence of this surplusage in the Indictment creates the risk that a jury could wrongfully convict Mr. Scrushy of breaching his common law, civil fiduciary duties or hold him responsible for the acts of others because he was "the highest ranking corporate officer." Even a meager chance of this occurring must be steadfastly avoided.

B. References to SEC Rules and Regulations Should Be Stricken From the Indictment

The Government's argument that the SEC "is a dual victim in this case" demonstrates that references in the Indictment to SEC rules and regulations are alleged for no other purpose than to inflame or confuse the jury. Opp. Br. at 14. Other than repeating its mantra that jury instructions cure all prejudice (Opp. Br. at 15), the Government does little to refute Scrushy's assertion that reference to civil regulations in the Indictment, which are not elements of the offenses charged, will confuse the jury and potentially lead to a criminal conviction based solely on a determination that Mr. Scrushy violated those SEC rules and regulations.

The Government contends that the "evidence will show that Scrushy knew that he was required to file certain financial documents with the SEC and knew that such documents would need to show falsely inflated earnings numbers or his scheme to pump up the value of HealthSouth stock would be disclosed." Opp. Br. at 14. But the alleged

scheme to "pump up the value of HealthSouth stock" *was* the filing of falsely inflated earnings numbers. To prove the offense charged, the Government would need to demonstrate, among other things, that Mr. Scrushy knowingly caused false financial statements to be filed, not that he knew that such false filing violated a discrete SEC rule or regulation. See 18 U.S.C. §§ 2, 1001, 1350(c)(2). Because Mr. Scrushy is not alleged to be criminally liable for violating SEC rules and regulations, the references to them are surplusage. See, e.g., United States v. Hasner, 340 F.3d 1261, 1269-70 (11th Cir. 2003) ("Although the indictment listed the state ethics statutes which purportedly prohibited Hasner from receiving the Chelsea Commons commission, the indictment did not rely upon violations of these state statutes as a basis for the honest services charges. Instead, the indictment focused on Hasner's unjust enrichment while he served as chairman of the HFA and on the concealment of Hasner's financial relationship with Fisher. Because the inclusion of the state statutes in the indictment was mere 'surplusage,' the district court's redaction of these statutes did not result in an impermissible broadening of the indictment.").

C. References to Superfluous Accounting Terms Should Be Stricken From The Indictment

The accounting terms and practices described in the Indictment plainly prejudice Mr. Scrushy. By including its own definitions of certain terms and, significantly, by failing to include definitions of a panoply of other accounting terms, the Government has effectively concluded for the jury what accounting terms are relevant to this case.

Indeed, even if after trial the jury is convinced that Scrushy's description of the relevant accounting terms and practices is correct, the jury still is likely to deliberate with the Government's pre-ordained definition in mind.

If, as it says, the Government "will take great care in explaining them at trial[]" (Opp. Br. at 17), the Government need not prejudice Scrushy by including those definitions in the Indictment. In this regard, the Government's reliance on United States v. Watts, 911 F. Supp. 538, 553 (D.D.C. 1995), is misplaced. While the Watts court concluded that the defendant's conduct needed to be "contextualized," this simply is not true here with regard to specific definitions of various accounting principles. The Government need only allege that there is such a thing as a balance sheet and that Mr. Scrushy caused false balance sheets to be filed. Explanations of the meaning of this and a whole host of other accounting terms should be provided through documents and testimony offered at trial by both parties, or as part of the Court's charge to the jury. Here, the Government seeks to preempt the evidence, and the role of the Court and the jury in deciding one of the central controversies in the case. The presence of these accounting definitions in the Indictment is prejudicial and unnecessary, and should be removed.

D. References to Mr. Scrushy's Alleged Conduct "Elsewhere" Should Be Stricken From The Indictment

The Indictment is rife with allegations that Mr. Scrushy engaged in various conduct within Jefferson County in the Northern District of Alabama, and "elsewhere."

Indictment at p. 6, ¶ 21; p. 11, ¶ unnumbered; p. 20, ¶¶ 3, 4, 3; p. 22, ¶¶ 3, 4; p. 24, ¶ 3; p. 25, ¶ 4, p. 26, ¶¶ 3, 4; p. 27, ¶ 2; p. 29, ¶¶ 2, 2; p. 30, ¶ 2; p. 31, ¶ 1. The Government defends these amorphous allegations by claiming that "the grand jury found, as it had the right to do, that Scrushy's fraud was wide-ranging and occurred in places that were not specifically described by the witnesses before it." Opp. Br. at 17. Mr. Scrushy and this Court are left to wonder how the grand jury issued an Indictment based upon alleged conduct not presented to it. But regardless of the motivations of this particular panel that the Government, in a rare moment of candor about grand juries, concedes made findings at the request of prosecutors without proof (Opp. at 17), the use of the term "elsewhere" in the Indictment is prejudicial because it gives the Government unfettered latitude to claim that Scrushy committed alleged criminal acts anywhere in the world. These allegations will necessarily be surplusage if the Government does not introduce evidence that Scrushy participated in the alleged fraud outside of "Jefferson County." Most importantly, however, reference to the term "elsewhere" throughout the Indictment creates the possibility that a jury could find him guilty of conduct not specifically alleged in the Indictment and for which he would have had no fair opportunity to mount a defense. Or, alternatively, in the event of an acquittal, Mr. Scrushy would be left to guess the conduct for which jeopardy attached. For these reasons, references to conduct that occurred "elsewhere" should be stricken from the Indictment.

III. Mr. Scrushy Is Entitled To Disclosure Of Information Regarding The Grand Jury Screening Process

Despite devoting seven pages of text to setting up a strawman that it eventually knocks down, the Government ultimately acknowledges that the relief sought by Mr. Scrushy -- an *in camera* review of the inquiries made to the grand jury members about their relationship to HealthSouth -- is appropriate. Unfortunately, the road to that admission is long and tortuous, filled with more gratuitous and self-serving descriptions about the charges pending against Mr. Scrushy. Along the way, the Government is unable to resist the temptation to take several cheap shots. Thus, while eager to avoid the Government's propensity to argue when there is no dispute, several clarifications need to be made.

In his motion, Mr. Scrushy does not suggest that grand jurors who had a relationship with HealthSouth would "necessarily be unable to determine whether probable cause existed to indict" him. Opp. Br. at 18. Nor does he claim that the grand jury was actually biased or that such bias should result in the dismissal of the Indictment. Opp. Br. at 22-24. Such scurrilous and speculative allegations, unsupported by proof, are left to the Government. Rather, Mr. Scrushy only seeks, consistent with the Constitutional protections afforded all defendants, to ensure that the process for determining whether the grand jurors could act fairly and impartially was adequate. See Bank of Nova Scotia v. United States, 487 U.S. 250, 257 (1988). Absent disclosure of the process utilized by the Government to prevent bias, neither counsel nor the Court

would be able to make any determination as to whether adequate steps were taken to ensure that an unbiased grand jury was empanelled.

Contrary to the Government's attempt to liken this case to a domestic terrorist attack, this is not a case like United States v. McVeigh, 896 F. Supp. 1549 (W.D. Okla. 1995) in which the defendant argues that all residents of the district are victims of the alleged crime and therefore biased. Rather, Mr. Scrushy contends that, because of the size of HealthSouth and its importance to this community, many members of the venire likely have strong feelings about (or actual connections to) the company and the recent disclosures about the conduct of some of its officers. It is essential, as the Government acknowledges, that this Court have an opportunity to review the process used by the Government to ensure that those strong feelings did not improperly taint the grand jury process. Mr. Scrushy defers to this Court's good judgment in determining, after *in camera* review of the grand jury screening process, whether his constitutional rights have been safeguarded.

IV. Mr. Scrushy Is Entitled To Have The Jury Determine Forfeiture Nexus

The Government concedes that Mr. Scrushy is entitled to have the jury determine forfeiture nexus. As such, there appears to be no dispute on this issue.

V. This Court Should Order That The Government Comply Fully With Rule 16(A)(1)(E)(ii)

As the Government eagerly notes, "the breadth, complexity, and duration of [the acts alleged in the Indictment] were of historically enormous proportions." Opp. Br. at

32. As a result, the Government's investigation has similarly yielded discovery materials of historically enormous proportions. To date, the Government has produced literally millions of pages of documents (in hard copy and electronic form) and hundreds of hours of video and audio tape. The Government has represented that the contents of the HealthSouth server alone, if printed and stacked page on top of page, would exceed the height of the Empire State Building. This massive volume of discovery materials does not include deleted emails and other files, which the Government has resurrected but has refused to produce on the grounds that they constitute "work product." Under such circumstances, it is essential that the Government be required to identify promptly the documents it intends to use at trial.

There is some debate in the federal courts about what precisely is required by Rule 16. As set forth in Mr. Scrushy's opening brief, several district courts have interpreted the literal language of Rule 16(a)(1)(E) as preventing the Government from using a broad brush approach to discovery, and instead requiring that the Government specify precisely which documents it intends to use at trial. See United States v. Poindexter, 727 F. Supp. 1470, 1484 (D.D.C. 1989); United States v. Turkish, 458 F. Supp. 874, 882 (S.D.N.Y. 1978); United States v. Upton, 856 F. Supp. 727, 747-48 (E.D.N.Y. 1994); United States v. Hsia, 2000 WL 195067, at *1 (D.D.C. Jan. 21, 2000). As the Government notes, several federal district courts have concluded otherwise. See

Opp. Br. at 29. While it appears that no federal appellate court and no court within this circuit has directly addressed the issue,[3] several federal appellate courts have recognized that the district courts have wide ranging inherent authority to regulate the nature and timing of discovery in criminal cases. See United States v. Washington, 318 F.3d 845, 857 (8th Cir. 2003); United States v. Cannone, 528 F.2d 296, 298 (2d Cir. 1975); United States v. Richter, 488 F.2d 170, 173 (9th Cir. 1973).

In support of its side of the debate, the Government relies heavily on United States v. Nachamie, 91 F. Supp. 2d 565 (S.D.N.Y. 2000).[4] However, the issue in Nachamie was whether the Government was required to distinguish which of the 200,000 documents produced were "material to the preparation of the defense," as required by Rule 16(a)(1)(E)(i), and which were documents that the Government intended to use at trial, as required by Rule 16(a)(1)(E)(ii). Here, the issue is not whether the Government has neatly segregated the documents mandated by Rules 16(a)(1)(E)(i) and (ii) into neat,

---

[3] Although the Government speculates that it is "highly probable" that the Court of Appeals for the Eleventh Circuit "would agree with these courts that have found no right to such information" (Opp. Br. at 29), it provides no explanation why the Court is more likely to follow the reasoning of one group of decisions from the Southern District of New York and District of Columbia than another group of decisions from the same courts, especially in a case with millions of pages of documents and no prejudice to the Government.

[4] At least one court has noted that Nachamie is inconsistent with the Second Circuit's holding in Cannone. See United States v. Lino, 2001 WL 8356, at *19 (S.D.N.Y. Dec. 29, 2000).

separate piles. Rather, the Government has produced millions of pages of documents representing a substantial portion of the files maintained at the headquarters of a Fortune 500 corporation, and has represented that "almost anything" could be used at trial. Opp. Br. at 32. In fact, the initial production by the Government contains massive quantities of wholly irrelevant material -- Happy Birthday emails, "get well" cards, copies of the 2002 University of Alabama football schedule, a Beanie Baby catalog, sorority induction rules --which could not possibly fall into any of the categories of Rule 16(a)(1)(E) and which the defendant must sort through, page by page, in order to reach the substantially smaller universe of potentially relevant documents that realistically could be used by the Government at trial or would be material to the preparation of Mr. Scrushy's defense. As even the Nachamie court would acknowledge, the Government does not satisfy its Rule 16 obligations by filling a tractor trailer with relevant and irrelevant documents and saying "its all there."[5]

---

[5] In fact, in Nachamie, the Court was so troubled by the onus placed on the defendant to find a needle in a haystack that it required the Government to serve a substantial bill of particulars in order to cure the fact that it had "not yet informed the defendants which of [the 2000 Medicare claims contained in the 200,000 documents] were false and the way in which they were false." Nachamie, 91 F. Supp. 2d at 571. In United States v. Alvarado, 2001 WL 1631396 (S.D.N.Y. Dec. 19, 2001) also cited by the Government here (Opp. Br. at 29), the Court addressed similar concerns by ordering the Government to provide defendants with a "witness list, the list of tapes to be used at trial and the index to the files which [would] enable each defendant to identify the alleged false and misleading statements or high pressure sales tactics, account

(Cont'd on following page)

Despite its protestations about the relief requested by Mr. Scrushy's motion, the Government sets forth a list of twenty categories of documents "some or all of which" it may use at trial but then notes that "it is conceivable that almost anything provided to the defense might be used for some purpose at some phase prior to trial." Opp. Br. at 31-32. While the value of the simultaneously underinclusive and overinclusive list provided by the Government is highly dubious, at best, the Government's willingness to provide such a list demonstrates that it acknowledges the need to take affirmative steps to ensure that a defendant has fair notice of the charges against him and the evidence that purportedly buttresses those charges. Unfortunately, the Government's offer does not go far enough.

This is not a garden variety case in terms of its complexity, scope or profile. Even if this Court is not persuaded that the literal language of Rule 16(a)(1)(E) or the weight of authority interpreting it mandates that the Government identify with specifity the documents it intends to use at trial, the Court has the discretion, in the exercise of its supervisory powers, to require more of the Government than is expressly provided by the rules. In other contexts, the rules of criminal procedure have been interpreted broadly to ensure fairness and to streamline preparation for and conduct of trial. See, e.g., United States v. Palermo, 2001 WL 185132 (S.D.N.Y. 2001) (directing that Jencks Act and

---

(Cont'd from preceding page)

information or other details required to prepare an adequate defense." Alvarado, 2001 WL 1631396, at * 5.

Giglio material should be produced in advance of trial, rather than after the witness testifies, as required by the rule, in order to prevent delay at trial); United States v. Ible, 630 F.2d 389, 395 (5th Cir. 1980) (acknowledging that under certain circumstances, attorney participation in voir dire may be appropriate); United States v. Price, 448 F. Supp. 503, 518 (D. Colo. 1978). Notions of fairness and due process do not permit the Government to bury a defendant in what is literally a mountain of paper and leave him (regardless of his claimed economic resources) to find a needle in a haystack. This is especially so where, as here, the Government is unable to demonstrate a scintilla of prejudice in being required to identify the documents it intends to use at trial, considering that it may reserve its right to modify that list as its trial strategy develops.

VI. The Government Should Be Ordered To Comply Fully With Its Discovery Obligations

While Mr. Scrushy is hopeful that the Government will comply fully with its discovery obligations, there are several disputed issues that may need to be resolved by this Court. The open discovery issues are as follows:

1. We have requested access to the "original" versions of various tape recordings so they can be tested by experts to determine if they are complete or have been tampered with.

2. The Government recently produced FBI 302 forms as part of its Brady and Giglio obligations. Those 302 forms have been redacted so as to exclude the dates of the interviews or the identities of the FBI agents who conducted them. We request that the

Government eliminate those redactions. We are prepared to make a separate, formal motion pursuant to Roviaro v. United States, 353 U.S. 53 (1957), if necessary, to address this issue.

3. The Government has taken the position that its efforts to resurrect deleted computer files (including emails) constitute work product and need not be disclosed. This creates the potential for trial by ambush in the event that the programs used by Mr. Scrushy's forensics experts do not uncover the same deleted files that the Government may use at trial. The Government should be required to produce copies of all deleted files that it has resurrected.

4. The Government has produced magnetic tapes that comprise the HealthSouth general ledger. Those tapes can only be reviewed on a Sun Microsystems Java server (which would cost several hundred thousand dollars to purchase). We have asked the Government to let us use its and/or HealthSouth's server to run searches on the general ledger for relevant information. The Government has not agreed to a mechanism that will enable Mr. Scrushy's counsel to review the data contained on those tapes.

Mr. Scrushy respectfully reserves his right to supplement the list of open discovery issues if and when they become ripe for this Court's consideration.

VII. Mr. Scrushy Is Entitled To A Hearing Regarding The Circumstances Of The Government's Surreptitious Taping

Mr. Scrushy's motion for a hearing seeks exactly that. But as with much of its opposition brief, the Government's response misses the point. Nowhere in his motion does Mr. Scrushy ask that the tape recordings be suppressed. Rather, he requests only that a hearing be held by this Court to determine whether the Government's conduct in directing William Owens to make those tape recordings surreptitiously, while Mr. Scrushy was represented by counsel, is sufficiently egregious to warrant suppression or other appropriate relief.

So fearful is the Government of having its conduct bared for public scrutiny that, in a reply brief in support of an unrelated discovery motion, it claims (gratuitously again) that the tape recordings "constitute powerful and insurmountable evidence of Scrushy's guilt." Government's Reply to Scrushy's Opposition to Government's Motion to Modify Discovery Order at ¶ 5. But neither hyperbole nor wishful thinking make it so. Contrary to the Government's claim, when the more than ten hours of tape recordings are heard in their entirety they demonstrate that Mr. Scrushy is innocent of the charges against him and show that he first learned from Owens that there were certain "problems with the numbers" (not that there was a wide-ranging fraud at HealthSouth) during the very same days that the recordings were made. And the Government knows this, so it seeks to prop

up its evidence preemptively through pithy sound bites that the media is all too quick to devour and regurgitate.[6]

While Mr. Scrushy is not afraid of the content of the tape recordings, he is fearful, as we all should be, of a Government that engages in unethical, "ends justify the means," conduct to try to build its case. The necessity of a hearing to determine the propriety of the Government's conduct is underscored by the disturbing admission contained in the Government's own opposition brief, that Owens was instructed to trap Mr. Scrushy into an admission of complicity for conduct he did not engage in.

As a threshold matter, the Government's effort to distinguish between the SEC's insider trading investigation on the one hand and the US Attorneys Office's investigation of accounting fraud on the other would be comical, were the implications not so serious. The Government claims that "the SEC was not investigating allegations of accounting fraud at HealthSouth; it was investigating allegations of insider trading" and that Mr. Scrushy only had "retained private counsel in connection with the insider trading allegations." Opp. Br. at 34. The SEC's own words at the beginning of Mr. Scrushy's March 14, 2003 testimony tell a very different story:

---

[6] The fact that the Government has repeatedly sent copies of the Indictment and its briefs (including its most recent reply on a simple motion to adjust the discovery scheduling order) to the press before serving counsel for Mr. Scrushy shows that its intended audience is neither the defendant nor this Court.

> "This is an investigation by the United States Securities and Exchange Commission in the matter of HealthSouth Corporation to determine whether there have been violations of certain provisions of the federal securities laws. However, the facts developed in this investigation might constitute violations of other federal, state, civil or criminal laws."

SEC Testimony at 7, a copy of which is attached hereto as Exhibit 1. Thus, the entire panoply of federal securities regulation was implicated and covered any and all conduct that could violate those laws.

Moreover, the transcript of Mr. Scrushy's SEC testimony is rife with questions and answers that have no bearing on the insider trading investigation, but are instead targeted directly towards the accounting fraud allegations that are now set forth in the Indictment. For example, Mr. Scrushy was asked the following questions and gave the following answers:

> "Q As part of your duties as the chairman and the CEO and these filings, was it your responsibility to sign off on various reports filed with the SEC?
>
> A I believe so.
>
> Q And what did that mean when you signed like quarterly reports or annual reports?
>
> A It was a requirement that we submit certain documents and myself and others I think had to sign it as well. So we submitted them and we all signed them as verified they were accurate.
>
> Q That what was accurate?
>
> A The reports. We were signing the documents, then submitting them because it was a requirement that we sign them and submit them.

Q Where did you learn that this was a requirement?

A From our attorneys.

Q In-house or out-house counsel?

A In-house. Well, in-house and out-house counsel, you're right. At that time we didn't have in-house counsel, we only had outside counsel.

Q When you signed that the reports were accurate, were you signing --

A I don't know that I -- obviously, I didn't -- couldn't sign off on accuracy on all those reports because number one, I'm not an accountant; number two, I'm not an attorney. They were submitted to me and I was told that I had to sign them as chairman and CEO of the company and I signed them.

Q Were you given the option that you did not have to sign them?

A No, sir. You have to sign them and submit them.

Q Did you ever ask anybody if you were allowed not to sign the reports?

A No. I was told we had to sign them and submit them as part of being a public company.

Q Did they tell you why you had to, why Richard M. Scrushy had to sign the reports?

A It was a requirement."

SEC Testimony at 27-28. Later in the transcript, the following exchange takes place:

"Q Would you have been given copies of the actual financial statements or -- well, let's take one at a time. Would you have been given copies or drafts of the actual financial statements included in this document?

A No.

Q Do you know what an income statement is?

A Yeah, I know what one is, sure.

Q How about a balance sheet, do you know what a balance sheet is?

A I know what it is.

Q Does the company or anybody ever provide it to you?

A I mean I look at it after it's been produced and all and I'll see it, you know, quarterly and whatnot. But I am not an accountant, so I don't -- I just take whatever they give me as being what it is. I certainly would have no ability to make any changes or manipulate it or do anything to it. I just take what they give me."

SEC Testimony at pp. 31-32.

Other instances of questioning regarding issues related to alleged accounting fraud abound. In fact, this Court can search in vain to find any testimony relating to insider trading in the first eighty two pages of the two hundred and thirty seven page transcript.[7] In addition, the Government has publicly stated that CMS Transmittal 1753,

---

[7] The Government claims that, "[i]n an effort to keep the two investigations separate, when [it] learned that the SEC was going to interview Scrushy under oath about the

(Cont'd on following page)

which formed the basis for the SEC's insider trading investigation, was used by the conspirators as a mechanism to conceal the accounting fraud which forms the basis for the Indictment, and has made specific reference to Transmittal 1753 in the Indictment. See Indictment ¶ 68.

Seeking to perpetuate the fiction of a distinction between the insider trading investigation and the accounting fraud investigation, the Government contends that "[i]t is inconsistent for Scrushy to claim that he was represented by counsel on allegations that he did not even know about." Opp. Br. at 34, n.10. But the Government's position turns the attorney-client relationship on its head. It is not for the Government to divine the scope of the representation that a lawyer agrees to provide to his client or that which the client has sought. Nor is it reasonable to anticipate that a lawyer retained to represent a client in connection with an insider trading investigation would pack up his briefcase and go home when the allegations or questions at a deposition shift to accounting fraud. Moreover, if the Government's allegations are true -- i.e., that Mr. Scrushy was the

---

(Cont'd from preceding page)

> insider trading allegations, it specifically asked that it not question him about the cash on hand and the manipulation of fixed assets at HealthSouth." Opp. Br. at 34 n. 9. Unfortunately, this narrowly-tailored admonition did not prevent the SEC from asking Mr. Scrushy about a host of other issues directly bearing on the accounting fraud claims that now form the basis for the Indictment. We doubt the Government will refrain from using Mr. Scrushy's statements to the SEC in this case because "the two investigations were kept separate."

mastermind of a multi-billion dollar accounting fraud -- surely Mr. Scrushy's retention of counsel would have accounted for all possible developments in the SEC investigation, including its discovery of the accounting fraud.

Another fact made abundantly clear by the Government's opposition brief is that the Owens tape recording was a set up. As the Government notes:

> "Owens was instructed by the FBI to wear a recording device and engage Scrushy in conversations . . . . Owens would tell Scrushy that Owens' wife knew about the fraud, had become angry, had said that she did not want Owens to go to jail, and had said that, if he signed any more false reports, she would divorce him."

Opp. Br. at 35. So the Government readily acknowledges that it hooked Owens up with a recording device, fabricated a lie about his wife's knowledge of the accounting fraud at HealthSouth and sent him off to try to entrap Mr. Scrushy into making an incriminating statement at a time when Mr. Scrushy was represented by counsel, and that such taping took place only days after Mr. Scrushy was questioned at length by the SEC regarding the accuracy of HealthSouth's financial statements and his role in reviewing and signing them.

Despite the desperation that tactic demonstrates and the odor of entrapment emanating from the Government's conduct in this case, which Mr. Scrushy's counsel first raised before the Honorable Inge P. Johnson during the asset freeze hearing conducted in April 2003, the Government claims that neither suppression nor a hearing on suppression is appropriate because (1) there is no legal authority for such a hearing and (2) the content of the Owens recordings is so "damning." The Government is wrong is both respects.

First, the Government makes much of the fact that Judge Clemons' decision in United States v. Bowman, 277 F. Supp. 2d 1239 (N.D. Ala. 2003) was vacated. But the unreported vacatur order was, on its face, predicated on the fact that a plea agreement had been reached and that the issue decided by the order -- i.e., that suppression was appropriate -- became moot.[8] Nothing in the vacatur order suggests that Chief Judge Clemons changed his mind about the reasoning behind the decision. Accordingly, the order vacating the decision is analogous to an appellate court reversing a district court's decision "on other grounds" but leaving the district court's view of the issue addressed intact. There is nothing to indicate that Judge Clemons' view of the law and the Government's conduct was not right or that it ceased to be the thinking of an experienced judge. In any event, there is ample other authority to support Mr. Scrushy's request for a hearing.

In United States v. Hammad, 858 F.2d 834, 838 (2d Cir. 1988), the United States Court of Appeals for the Second Circuit held that ABA Model Code of Professional Responsibility 7-104(A)(1) (the predecessor to Model Rule 4.2), which prohibits a lawyer from communicating with a party known to be represented by counsel, applies to the

---

[8] Although the Government is correct that it advised counsel for Mr. Scrushy of the "vacated status" of the decision, it fails to note that counsel responded by indicating that the vacatur was based on a plea agreement, not a change of heart by Judge Clemons. A copy of the letter from Abbe David Lowell to Richard Smith dated February 3, 2004 is attached hereto as Exhibit 2.

investigatory stages of a criminal prosecution prior to the attachment of Sixth Amendment protections. As the Second Circuit noted,

> "[t]he Constitution defines only the 'minimal historic safeguards which defendants must receive rather than the outer bounds of those we may afford them. In other words, the Constitution prescribes a floor below which protections may not fall, rather than a ceiling beyond which they may not rise. The Model Code of Professional Responsibility, on the other hand, encompasses the attorney's duty 'to maintain the highest standards of ethical conduct.' The Code is designed to safeguard the integrity of the profession and preserve public confidence in our system of justice. It not only delineates an attorney's duties to the court, but defines his relationship with his client and adverse parties. Hence, the Code secures protections not contemplated by the Constitution. Moreover, we resist binding the Code's applicability to the moment of indictment. The timing of an indictment's return is substantially within the control of the prosecutor. Therefore, were we able to construe the rule as dependent upon indictment, a government attorney could manipulate grand jury proceedings to avoid its encumbrances."

Id. at 839 (internal citations omitted). The Court concluded that "in light of the underlying purposes of the Professional Responsibility Code and the exclusionary rule, suppression may be ordered in the district court's discretion" to remedy an ethical breach. Id. at 840. Other circuits have similarly included suppression among the panoply of remedies available to district court judges for violations of DR 7-104(A)(1). See United States v. Killian, 639 F.2d 206, 210 (5th Cir. 1981), cert. denied, 451 U.S. 1021 (1981) (holding that "[s]uppression of the statements would probably have been the appropriate sanction in this case, were it not for the refusal of the Government to use those statements"); United States v. Durham, 475 F.2d 208, 211 (7th Cir. 1973) (suppressing evidence as the result of "ethical questions" arising from statements taken in the absence

of retained counsel); United States v. Thomas, 474 F.2d 110112 (10th Cir.), cert. denied, 412 U.S. 932 (1973) (holding that suppression of evidence obtained in a manner violative of the ethical canons is mandatory). See also United States v. Sam Goody, Inc., 518 F. Supp. 1223, 1224-25 n.3 (E.D.N.Y. 1981) (holding that "it was unethical for the Government to 'wire' an informant and send him to one of the defendants' offices in an attempt to elicit incriminating statements from him after that defendant's attorney had presented himself. . . . "). The McDade amendment was enacted to codify the requirement, applied in the aforementioned cases, that attorneys for the Government be bound by state laws and rules, and local federal court rules that apply to the conduct of all other attorneys. See Bowman, 277 F. Supp. 2d at 1242.

Notably, the Government does not cite to a single case, within this Circuit or elsewhere, which holds that a suppression hearing is an inappropriate mechanism to consider the ethics of the Government's conduct. Rather, the pre-McDade Amendment cases cited by the Government (Opp. Br. at 41) stand for the unremarkable proposition that certain courts, usually applying federal law, once turned a blind eye to conduct for which Congress has since sought to hold Government lawyers accountable pursuant to relevant state law. See, e.g., United States v. Plumley, 207 F.3d 1086, 1095 (8th Cir. 2000) ("Although this statute [28 U.S.C. § 530B] may inform our approach to future cases such as this, we need not consider it here because it did not become effective until April 21, 1999, well after the June 9, 1998, contact between Kaune and Bricko. In the meantime, we agree with those courts that have concluded that the interpretation of state

disciplinary rules as they apply to federal criminal law practice 'should be and is a matter of federal law.'"). And, unlike the Bowman case, none of the pre-McDade Amendment cases cited by the Government purport to apply Alabama law, as Section 530B requires in this case. That, to be sure, is why the Government has run away from Bowman and into the arms of pre-McDade Amendment law from other jurisdictions.

Those cases, applying "federal law" or the law of sister states, are of little help to the Government. For example, in United States v. Balter, 91 F.3d 427, 436 (3d Cir. 1996), the court first concluded that New Jersey's Rule 4.2 only applied to a "'party' represented in a 'matter.' A 'party' is necessarily a 'party' *to* something." Balter, 91 F.3d at 436. This conclusion, however, is directly contrary to Alabama law. See Comment to Alabama Rule 4.2 ("This rule also covers any person, *whether or not a party to a formal proceeding*, who is represented by counsel concerning the matter in question.") (emphasis added). The Balter court then concluded that "New Jersey case law has explicitly exempted ordinary pre-indictment investigation as within the 'authorized by law' exception to the Rule." Balter, 91 F.3d at 436 (citation omitted). There is, of course, no support in Alabama law for such a conclusion; otherwise the Government no doubt would have directed this Court to it. To the contrary, the Bowman case, which is the only case we could find that addresses this issue under Alabama law, unequivocally concluded that contact similar to the government's here was *not authorized by law.*

The Government should similarly find little solace in a case like United States v. DeVillio, 983 F.2d 1185 (2d Cir. 1993), which, at the very least, recognizes the "potential for prosecutors to overstep the broad powers of their office and in doing so, violate the ethical precepts of DR 7-104(A)(1)" (DeVillio, 983 F.2d at 1192), and that a determination regarding the nature of the Government's conduct should be assessed on a case by case basis. See, e.g., DeVillio, 983 F.2d at 1192 ("However, *in the instant case*, there is no evidence of any violation rising to the level of the one we considered in Hammad.") (emphasis added). The need for the Court to hold a hearing in this case is particularly acute because, from the inception of the Government's attempt to get Richard Scrushy at any cost, it has crossed the ethical line. See SEC v. HealthSouth Corp., 261 F. Supp.2d 1298 (N.D. Ala. 2003).

The Government -- clearly unsated in its appetite for making extrajudicial statements and including cheap shots in filings with the goal of trying its case in the media -- also claims that the tapes should not be suppressed because they contain a "spate of damning admissions." The Government then lays out these supposed "damning admissions" in a series of out of context snippets taken from more than ten hours of surreptitious recordings.[9] Of course, this Court's determination as to whether evidence

---

[9] Even scant attention to where the Government uses quotation marks and where it does not will reveal the transparency of its effort to manipulate the context of Mr. Scrushy's statements to Owens.

should be suppressed or whether a hearing should be held cannot rest on whether the evidence at issue is damning, vindicating, ambiguous or just plain irrelevant. The Government seems to seek a special rule in Alabama that the degree of Constitutional protection a person gets depends on how guilty the Government claims he is. This novel approach flies in the face of every Supreme Court decision from Mapp v. Ohio, 367 U.S. 643 (1961), to Gideon v. Wainwright, 372 U.S. 335 (1963), to Miranda v. Arizona, 384 U.S. 436 (1966). Rather, it is the conduct of the Government in obtaining the surreptitious evidence that matters. See, e.g., United States v. Best, 135 F.3d 1223, 1224-25 (8th Cir. 1998); United States v. Freeman, 579 F.2d 942, 947-48 (5th Cir. 1978); United States v. Greathouse, 2003 WL 23110388 (D. Or. Oct. 20, 2003). Despite the irrelevancy of the content of the potentially suppressible evidence, Mr. Scrushy feels obliged to direct the Court's attention to just a handful of the excerpts of testimony that suggest he only learned that there were problems with the numbers as the result of his (unbeknownst to him recorded) conversations with Owens.

Notably, throughout the recording that he did not know was occurring, Mr. Scrushy makes reference to "you," meaning Owens, in discussing what Owens was describing as fraud at HealthSouth. For example, after Owens subtly tries to suggest that something is amiss, it is Mr. Scrushy who says to Owens "[y]ou ought to be able to engineer your way out of what you engineered your way into" (Transcript at 30, attached hereto as Exhibit 3); "it seems you are already in it, Bill. I don't see you getting out of it" (Transcript at 30); and "I think you ought to go down fighting, Bill. You ought to go

down fighting. You know what I mean? Try doing the right thing, you ought to go down fighting." Transcript at 31. Other examples abound. Nowhere does Mr. Scrushy state or suggest that he was involved in the fraud or even knew about it before Owens disclosed to him a day earlier that there were problems with the numbers.[10] In fact, in an earlier recorded conversation, Mr. Scrushy asks Owens whether there is anything in the numbers that he needs to be concerned about.[11] Tellingly, Owens responds, in the negative. Perhaps most enlightening, however, is Mr. Scrushy's statement, made in response to Owens' suggestion that HealthSouth engage in an aggressive accounting tactic, that "we are not going to report one more penny then we earned."

In short, Mr. Scrushy is confident that a complete and in context reading or hearing of the surreptitious Owens recordings will indicate that Mr. Scrushy was unaware of Owens' conduct. The tapes will also serve to show how desperate the Government was to trap Mr. Scrushy on the very day before they purportedly had "probable cause" to conduct a raid and make arrests. The tapes will also serve to show how, through its all too willing agent, the Government lied and twisted to get Mr. Scrushy to say something

---

[10] At the conclusion of the SEC asset freeze hearing last spring, Judge Johnson found the statements contained in the tape to be "ambivalent at best." HealthSouth, 261 F.Supp.2d at 1329.

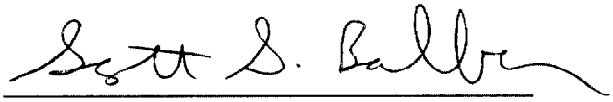
[11] Unfortunately, these earlier conversations have not yet been transcribed and the Government conveniently ignores their existence when it seeks to tar Mr. Scrushy with the contents of the tapes.

that it now claims it had all along -- real evidence of wrongdoing. Finally, the tapes will show that Mr. Scrushy did not take the bait no matter how hard Owens (and the Government) tried. Notwithstanding the truth about the actual contents of the tape recordings, Mr. Scrushy is entitled to the protections afforded by the Constitution and the laws of this land, and a hearing is warranted to ensure that those protections are safeguarded, in their entirety.

CONCLUSION

For all the reasons set forth herein, and in Mr. Scrushy's opening brief, this Court should grant Mr. Scrushy's motions in their entirety.

DATED: February 17, 2004



Abbe David Lowell
Thomas V. Sjoblom
Scott S. Balber
Chadbourne & Parke LLP
1200 New Hampshire Avenue, N.W.
Washington, D.C. 20036

Arthur W. Leach
c/o Thomas, Means, Gillis & Shay, P.C.
H. Lewis Gillis
Raymond L. Johnson Jr.
505 20th Street North
Birmingham, Alabama 35237

Attorneys for Defendant
Richard M. Scrushy

SEE FILE FOR EXHIBITS